

MEMORANDUM

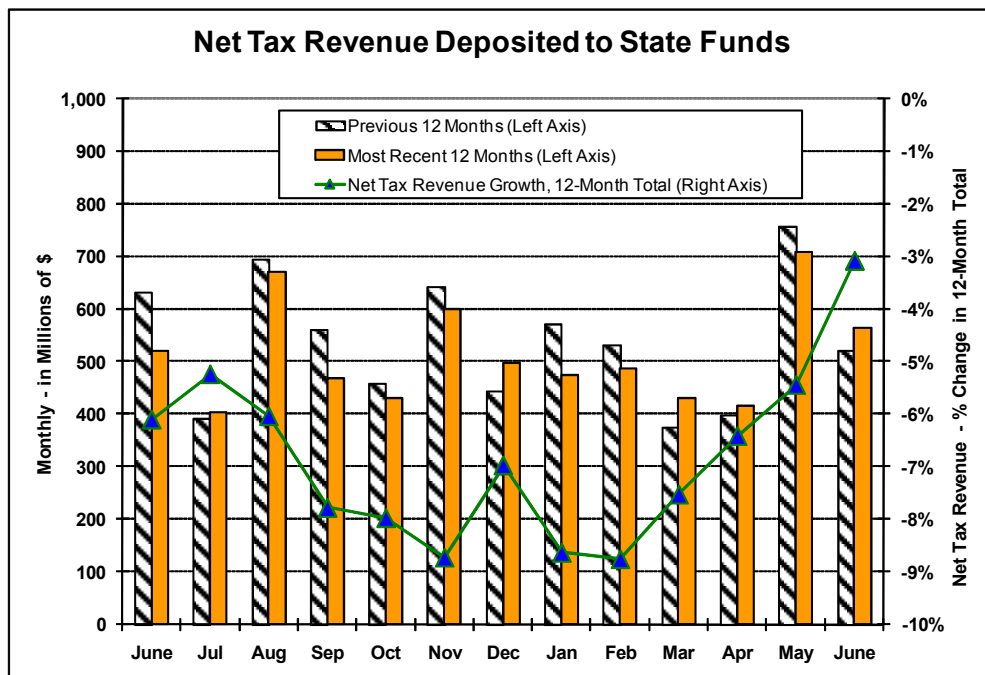
TO: Members of the Iowa Senate and
Members of the Iowa House of Representatives

FROM: Jeff Robinson
Shawn Snyder

DATE: July 22, 2010

Twelve-month Total Net Tax Receipts Through June 30, 2010

The attached spreadsheet presents net tax revenue deposited to State funds for the 12-month period ending June 2010 with comparisons to the previous twelve months. June 2009 to June 2010 one-month comparisons are also presented. The source of the information is the State accounting system, including non-General Fund accounts. All accounting transactions related to taxes remitted to the State were reviewed, along with the refunds issued against those taxes.



Month of June Comparison

June net tax receipts totaled \$564.1 million, an increase of \$44.3 million (8.5%) compared to June 2009. Major taxes and their contribution to the month's change include:

- Individual Income Tax (positive \$40.4 million, 20.0%) – Gross income tax receipts increased \$23.4 million in June while income tax refunds decreased \$17.0 million. The large increase

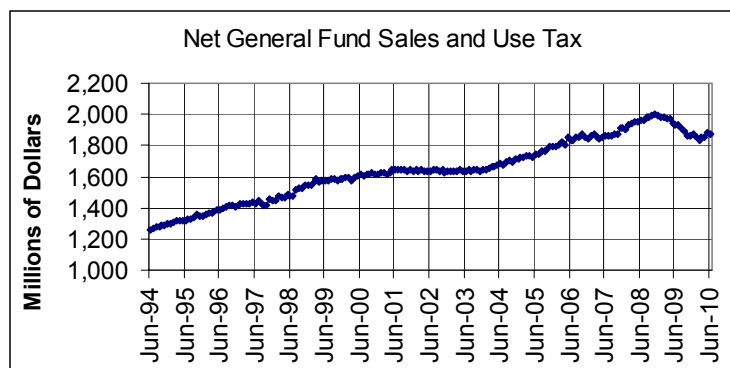
in net revenue was due to significant differences in how tax year 2009 income tax returns were processed this spring compared to last spring and the June increase offsets a similar decrease in May.

- Sales/Use Tax (negative \$0.3 million, - 0.2%)
 - Road Use Tax Fund use tax/fees for new registrations increased \$4.0 million, the third straight month of strong growth.
 - Gross General Fund sales/use tax receipts decreased \$5.2 million and refunds issued for the month decreased \$0.8 million (net decrease of \$4.4 million).
- Corporate Income Tax (positive \$0.8 million, 2.0%) – Gross corporate tax receipts decreased \$5.6 million and refunds decreased \$6.4 million.
- Fuel Tax (negative \$10.1 million, - 22.9%) – Gross fuel tax revenue decreased \$9.5 million while refunds processed in the month increased \$0.6 million. Deposit timing likely played a role in the large June decrease.
- Cigarette and Tobacco Taxes (positive \$3.9 million, 19.5%) – Deposit timing contributed to the large June increase.
- Gambling Tax (positive \$0.4 million, 1.7%) – Total adjusted gross revenue for Iowa's 17 State-regulated gambling facilities increased 0.1% in June 2010, compared to June 2009, and gambling tax revenue recorded positive growth for the first time in 16 months.

Year-over-Year Comparison – Net Tax Revenue

During the 12-month period ending June 2010, net revenue from all taxes deposited to State funds totaled \$6.146 billion, a decrease of \$195.8 million (- 3.1%) compared to the prior 12 months. Major contributors to the year-over-year dollar and percentage changes include:

- Individual Income Tax (negative \$86.3 million, - 3.2%) – The rate of individual income tax receipt growth peaked in May 2008 at 11.8% year-over-year. The annual growth rate bottomed at negative 9.3% in February 2010 and has recovered significantly, but growth remains negative.
- Sales/Use Tax (negative \$57.1 million, - 2.6%) – While the annual growth in sales/use tax revenue is still quite negative, it is a significant improvement from the negative 7.4% over the twelve months ending February 2010. At that point, net sales/use tax revenue was 8.4% below its November 2008 peak. The following graph presents an historical picture of the General Fund portion of sales/use tax.



- Corporate Tax (negative \$42.5 million, - 16.9%) – The most recent twelve months have produced \$208.6 million in net corporate income tax, down \$163.2 million (- 43.9%) from its June 2008 peak.
- Fuel Tax (positive \$19.9 million, 4.8%) – An irregular deposit impacting July 2008 causes the 12-month increase in fuel tax revenue to be significantly higher than is actually the case. According to Department of Revenue fuel sales reports, over the most recent 12-month period Iowa taxable gasoline/ethanol gallons sold increased 1.9% while taxable diesel sales were down 2.4%, the twentieth consecutive month showing a decline in annual taxable diesel sales. Taxable diesel sales over the most recent 12-month period were 9.4% below the March 2008 peak sales level.
- Gambling Tax (negative \$10.9 million, - 3.7%) – Despite expansions of casinos in Clinton and Dubuque, two changes providing boosts to year-over-year gambling growth in Iowa; gambling tax revenue is negative over the past twelve months. According to Racing and Gaming Commission statistics, twelve of Iowa's seventeen casino/track locations reported negative annual adjusted gross revenue (AGR) growth for the 12-month period ending June 2010. The AGR growth for all facilities was negative 3.4% over the past twelve months. Excluding the two expanded facilities, growth was negative 4.2%.
- Cigarette and Tobacco Tax (negative \$6.8 million, - 2.9%) – Economic conditions, Iowa's indoor smoking ban, and an increase in the federal cigarette tax are potential contributors to the tax revenue decline.
- Insurance Premium Tax (positive \$0.1 million, 0.1%) – The first insurance premium tax payment is collected in June and June 2010 was considerably higher than June 2009. The increase is likely the result of fewer redemptions of tax credit certificates compared to last year.

Tax Spotlight – Sales and Use Tax

Sales of goods and services to the final user are taxed under the authority of Iowa Code Chapter 423. The sale of all tangible property to the final user is subject to tax unless the tangible property is specifically exempt in Iowa Code Section 423.3. The sale of services is exempt unless specifically enumerated in Iowa Code Section 423.1(6). With a few exceptions, items that are exempt from sales tax are also exempt from use tax.

The State sales tax rate was increased to 6.0% with one-sixth of the tax devoted to school infrastructure in 2008. With the increase in the State sales tax rate, the school infrastructure local option (SILO) sales tax was repealed (this local option tax was initiated in HF 2282, Local Option Sales Tax for School Infrastructure Act of 1998). In addition to the State sales tax, with voter approval, local jurisdictions can impose a local option sales tax (LOST) of up to 1.0% (see HF 395, Local Option Sales Tax Act of 1985).

The use tax (Consumer and Retailer) rate was also increased to 6.0% in 2008, with one-sixth of the tax devoted to school infrastructure. The motor vehicle use tax remains at 5.0%. The use tax is not subject to LOST (except for transactions involving natural gas, natural gas services, electricity, or electric service). In general, the use tax includes:

- Tax collected by out-of-state based firms making sales of tangible personal property or certain services purchased for use in Iowa (retailer's use tax).

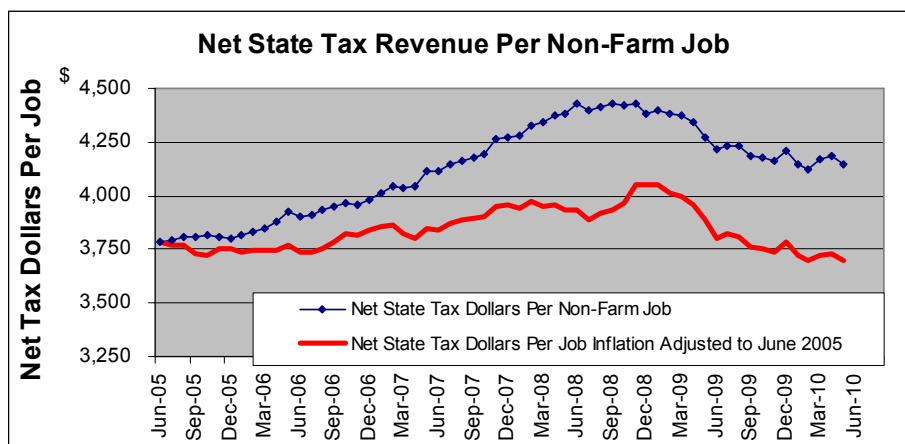
- Tax on goods or services purchased tax free by consumers and subsequently used in Iowa (consumer's use tax).
- Tax collected by Iowa county treasurers or the Iowa Department of Transportation on vehicles subject to registration (motor vehicle use tax).

The Iowa sales tax was first imposed in 1934 in HF 1 (Net Income and Retail Sales Tax Act) for a three-year period at a rate of 2.0%. The tax was made permanent in 1937 with the passage of SF 316 (Sales Tax Act). The Iowa use tax was enacted in 1937 (SF 317 – Use Tax Act) in conjunction with the permanent adoption of the sales tax at the 2.0% rate. The tax rates were increased to 2.5% in 1955, lowered to 2.0% in 1957, increased to 3.0% in 1967, and 4.0% in 1983. The rate was changed to 5.0% in 1992. During the 2008 Legislative Session, the SILO sales tax was repealed and replaced with the 1.0% point increase in the State sales/use tax in HF 2663 (State Sales/Use Tax for School Infrastructure Act of 2008).

Retailers selling tangible personal property or taxable services are responsible for collecting the State sales tax and any local option sales tax. The retailers are required to hold a retail permit and file a tax return. Depending on the amount of tax collected, deposits are due annually, quarterly, monthly or semi-monthly. State sales tax is deposited in the State General Fund. State sales/use tax for school infrastructure and LOST are initially deposited to the State General Fund and are transferred to special funds near the end of the month. Disbursements to local entities imposing the tax are made monthly from the special funds.

Tax Revenue and Employment

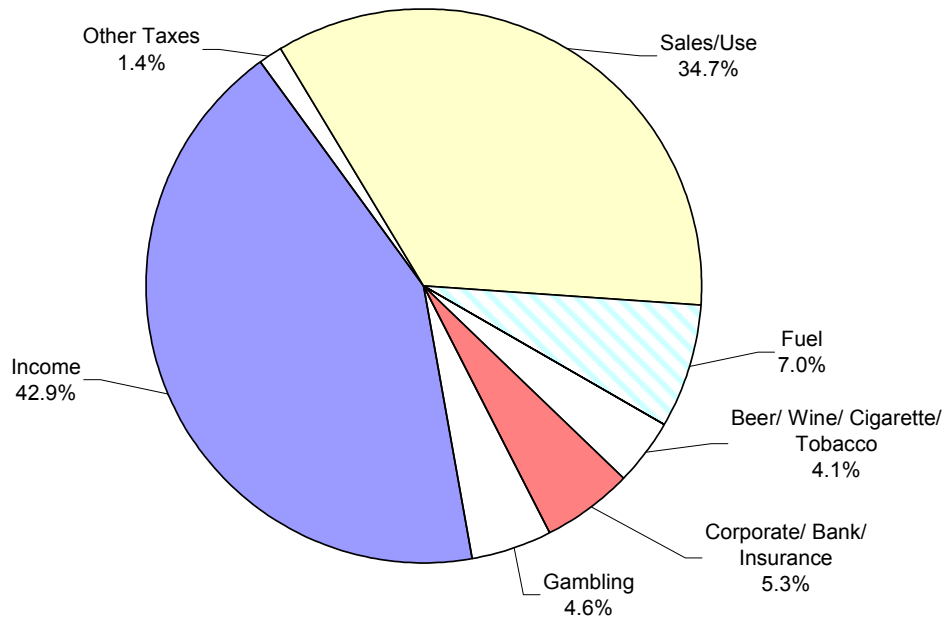
The average reading for Iowa non-farm employment over the 12 months ending May 2010 is 1,470,400, and net State tax receipts over the same twelve months totaled \$6.101 billion, or \$4,149 per non-farm job. This is \$365 (9.6%) higher than the per-job average for the twelve months ending July 2005. Over that same time period, inflation (CPI-U) increased 12.2%. Therefore, tax revenue per job has trailed the rate of inflation since July 2005 by roughly 0.5% per year. The following chart provides a historical perspective of tax collections per non-farm job and inflation-adjusted collections per job.



Net State Tax Revenue - Twelve Months Ending June 2010

Net Revenue = \$6.146 Billion

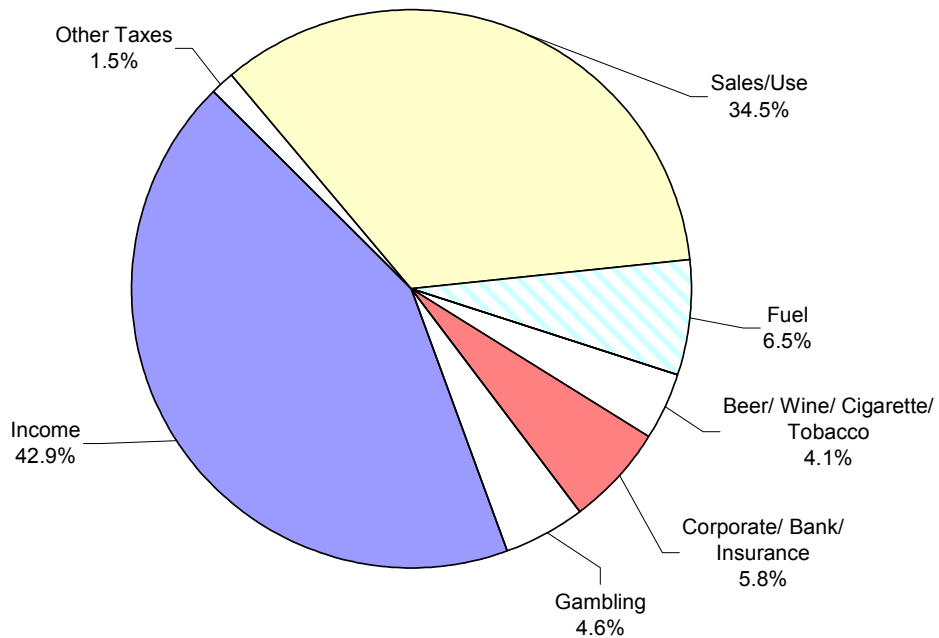
Percentages may not add to 100% due to rounding



Net State Tax Revenue - Twelve Months Ending June 2009

Net Revenue = \$6.341 Billion

Percentages may not add to 100% due to rounding



Net Tax Revenue Deposited to State Funds - Cash Basis

Dollars in millions - Columns and Rows may not add due to rounding

Net Tax by Tax Type	Previous 12-Month Period Total	Most Recent 12-Month Period Total	12-Month \$ Change	12-Month % Change	Month of June 2009	Month of June 2010	June \$ Change	June % Change
Banking	\$ 28.7	\$ 27.4	\$ - 1.3	-4.5%	\$ 4.7	\$ 5.3	\$ 0.6	12.8%
Beer & Wine	20.9	21.1	0.2	1.0%	1.9	1.8	- 0.1	-5.3%
Cigarette & Tobacco	238.2	231.4	- 6.8	-2.9%	20.0	23.9	3.9	19.5%
Corporate Income	251.1	208.6	- 42.5	-16.9%	40.2	41.0	0.8	2.0%
Fuel	412.7	432.6	19.9	4.8%	44.1	34.0	- 10.1	-22.9%
Gambling	293.3	282.4	- 10.9	-3.7%	22.9	23.3	0.4	1.7%
Individual Income	2,722.7	2,636.4	- 86.3	-3.2%	202.5	242.9	40.4	20.0%
Inheritance	73.7	65.9	- 7.8	-10.6%	6.8	6.3	- 0.5	-7.4%
Insurance	88.4	88.5	0.1	0.1%	15.4	25.5	10.1	65.6%
Other Taxes	8.9	7.3	- 1.6	-18.0%	1.8	0.6	- 1.2	-66.7%
Real Estate Transfer	14.8	13.1	- 1.7	-11.5%	1.0	1.3	0.3	30.0%
Sales/Use	2,188.0	2,130.9	- 57.1	-2.6%	158.5	158.2	- 0.3	-0.2%
Total Net Taxes	\$ 6,341.4	\$ 6,145.6	\$ - 195.8	-3.1%	\$ 519.8	\$ 564.1	\$ 44.3	8.5%
Gross Tax & Refunds								
Gross Tax	\$ 7,577.9	\$ 7,402.8	\$ - 175.1	-2.3%	\$ 609.5	\$ 629.4	\$ 19.9	3.3%
Tax Refunds	\$ - 1,236.5	\$ - 1,257.1	\$ - 20.6	1.7%	\$ - 89.7	\$ - 65.2	\$ 24.5	-27.3%
Net Tax Receipts by Fund								
State General Fund (GF)	\$ 5,418.8	\$ 5,220.6	\$ - 198.2	-3.7%	\$ 432.4	\$ 482.4	\$ 50.0	11.6%
Road Use Tax Fund	\$ 671.8	\$ 691.1	\$ 19.3	2.9%	\$ 64.1	\$ 57.9	\$ - 6.2	-9.7%
Non-GF Gambling	\$ 231.4	\$ 214.8	\$ - 16.6	-7.2%	\$ 22.7	\$ 23.1	\$ 0.4	1.8%
Other State Funds	\$ 19.3	\$ 19.2	\$ - 0.1	-0.5%	\$ 0.7	\$ 0.8	\$ 0.1	14.3%
Local Option Taxes *	\$ 798.1	\$ 780.5	\$ - 17.6	-2.2%	\$ 68.0	\$ 68.1	\$ 0.1	0.1%

* Sales, income, and hotel/motel. Distributed to local governments - not included in numbers above.

Numbers are rounded to the nearest \$0.1 million. Percentages are calculated after rounding.

Tax Categories Used in Table

Franchise (Bank) Tax: Taxes on banks are deposited to the State General Fund. State credit union tax is included on this line also.

Beer & Liquor Tax: Taxes on beer, liquor, and wine are deposited to the State General Fund, the Liquor Control Fund, and a small amount is deposited to a Department of Economic Development fund for wine promotion.

Cigarette & Tobacco Tax: Cigarette and the tobacco products tax revenue is deposited to the State General Fund.

Corporate Income Tax: All corporate tax is deposited to the State General Fund.

Motor Vehicle Fuel Tax: All motor vehicle fuel tax is deposited to one of two road use funds, with the exception of tax revenue from the sale of aviation and marine fuels.

Gambling Tax: The first \$6.0 million of gambling tax revenue each fiscal year is deposited to the State General Fund (increased to \$66.0 million beginning FY 2010). Other funds receiving deposits of gambling tax revenue over the last 24 months include the School Infrastructure Fund, the Rebuild Iowa Infrastructure Fund, the Gambler's Assistance Fund, the County Endowment Fund, and the Vision Iowa Fund.

Individual Income Tax: Most individual income tax revenue is deposited to the State General Fund. A total of \$4.0 million per year is deposited to the Workforce Development Fund. An annual \$2.6 million diversion to the Child Daycare Fund ended in FY 2009. In addition, several economic development programs are financed by individual income tax withholding. In those instances, the employer does not remit the tax withheld from employees and it is never deposited to a State fund. That revenue is not included here.

Inheritance Tax: All inheritance tax is deposited to the State General Fund.

Insurance Premium Tax: All insurance premium tax is deposited to the State General Fund.

Other Taxes: Other taxes include brucellosis eradication property tax (deposited to a Department of Agriculture and Land Stewardship fund), drug stamp tax (State General Fund), utility replacement property tax (State General Fund), and car rental tax (Road Use Tax Fund). Other taxes also include a suspense account used to hold tax deposits prior to determining the correct tax type for the money and tax revenue transferred by the Department of Revenue to separate accounts to fund tax collection activities (tax gap and Department operations).

Real Estate Transfer Tax: Real estate transfer tax is collected by counties. Counties retain 17.25% and remit the remainder to the State. The State deposits 90.0% to the State General Fund, 5.0% to the Housing Trust Fund, and 5.0% to the Shelter Assistance Fund. The distribution of real estate transfer tax revenue changed in FY 2010, when the State General Fund percentage begins a decline to 65.0% by FY 2015.

Sales/Use Tax: General sales/use tax is deposited to the State General Fund, while most vehicle use tax is deposited to the Road Use Tax Fund. Beginning FY 2009, the vehicle use tax was converted to a fee structure. To allow continuity of data, revenue from the fee structure is reflected in this document as tax revenue. Also beginning FY 2009, the School Infrastructure Local Option (SILO) sales tax was converted to a statewide 1.0% sales/use tax and the revenue from that statewide tax is transferred out of the State General Fund monthly through a refund appropriation. To allow for continuity of data, the refund transfers are subtracted as part of the net sales/use tax calculation.

Local Option Taxes: Local option taxes are presented at the bottom of the table and are not included in the numbers above. Prior to FY 2009, local option taxes included the SILO tax, Local Option Sales Tax (LOST) for local government finance, Local Option Income Surcharge for schools, and hotel/motel tax. Starting FY 2009, the SILO tax was converted to a 1.0% statewide tax and the SILO was eliminated. To allow for continuity of data, the transfers from the State General Fund as a result of the 1.0% statewide tax are included in the local option tax amount.

Report Database

The database for this report is the State accounting system. If transactions are incorrectly coded in the system as tax revenue or tax refunds, the numbers presented here will be impacted.